DOE Negotiates Ruling To Help Minority Businesses Compete In Natural Gas Market, Banks Improve Community Investment Rating

Small and disadvantaged businesses, including women and minority-owned, can now step into the competitive $90 billion natural gas market thanks to the U.S. Department of Energy and a ruling from the Treasury Department's Office of the Comptroller of the Currency.

DOE's Office of Fossil Energy and Office of Economic Impact and Diversity worked with Union Bank of California and minority-owned business, Visage Energy, to persuade the Comptroller of the Currency to look more favorably on those banks that offer disadvantaged, minority firms financial help through a new, low-cost credit agreement.

The Energy Department advocated the cause of small, minority-owned businesses with the Federal banking regulators, winning a favorable ruling last November. The Comptroller of the Currency's ruling bolsters the competitive opportunities for minority businesses while also giving U.S. banks the incentive to assist these firms. In turn, the banks have the opportunity to improve their ratings with regulators who track community investments of financial institutions.

Small businesses operate on a shoestring, but they power the U.S. economy. Across the Nation 23 million small businesses employ more than 50 percent of the Nation's private workforce. Combined, they generate more than half of the nation's gross domestic product and provide the principal source of new jobs.

However, small, disadvantaged businesses seeking to market natural gas find their financing and credit needs far exceed their credit resources. Typically producers want a letter of credit to guarantee payment for the gas they supply to the marketer and marketers are required to have strong balance sheets to support a letter of credit to execute a short-term natural gas contract. Most of these minority firms cannot overcome such steep financial hurdles. This prevents many small companies from competing in the natural gas marketplace.

The Energy Department saw a solution to this roadblock in the steps one minority-owned natural gas marketer took with his bank. Will Johnson, the Chairman of Visage Energy, in Culver City, CA, teamed up with Union Bank of California to design a Funds Transfer Agent Agreement, a financial instrument that transfers the minority firm's credit risk to the natural gas purchaser.

Through the use of the Funds Transfer Agent Agreement, small and disadvantaged companies, now have credit opportunities to compete in the natural gas marketplace.

Banks are currently rated for their community investment activity under the Community Reinvestment Act, a law enacted by Congress in 1977 and revised in May 1995. The Community Reinvestment Act (CRA) requires that each bank's record in helping meet the credit needs of its entire community be evaluated periodically. Late last year the Office of the Comptroller of the Currency ruled it will give favorable CRA consideration to financial institutions that assist small and disadvantaged businesses with a Funds Transfer Agent Agreement.

But banks must first satisfy certain Federal regulations. To comply with the Community Reinvestment Act the bank must meet three criteria:

1. Have as its primary purpose community development;
2. Provide a service that is related to the provision of financial services; and
3. Provide a service that has not been considered in the evaluation of the institution's retail banking services.

The Office of the Comptroller of the Currency ruled on November 25, 1998, in its first application of the Funds Transfer Agent Agreement to a bank's Community Reinvestment Act rating, that Union Bank of California met all three criteria in its work with Visage Energy. This opens a door to other small, minority-owned businesses and to banks throughout the U.S.

The way the Funds Transfer Agent Agreement works, the small business first identifies a natural gas supplier and a utility, or other potential buyer, to buy the natural gas. The marketer then locates a bank willing to act as its agent in the transaction. The marketer signs a Funds Transfer Agent Agreement with the bank, making the bank its agent. The marketer then includes this agreement in the natural gas purchase and sales contracts it signs with the two businesses.

The bank then acts as an intermediary, establishing a “blocked” account. The account is set up in the name of the minority business but is strictly controlled by the bank. The bank accepts a wire transfer payment from the buyer of the natural gas, typically a utility. It wires the correct payment to the natural gas producer and then moves the profits over to the operating account for the minority-owned business.

The agreement gives the utility-buyer an opportunity to improve its portfolio of purchases from minority-owned businesses. Some local distribution companies openly commit to buying 20 percent of their fuel supplies from minority-owned businesses. The agreement also allows a large producer who may already supply the utility with a percentage of its supplies a chance to have a cut of the 20 percent minority-owned business opportunity by selling natural gas to a small, disadvantaged marketer to resell to the utility without incurring the higher level of risk associated with smaller companies.

The Funds Transfer Agent Agreement includes signed contracts that the producer will sell at a certain price, and the utility will buy at a price slightly above the producer's selling price, leaving the small natural gas marketer with a profit and money to pay the agreed upon bank fee. The “blocked” account protects the producer and ultimate purchaser, eliminating the credit risk for the small business and enabling small and disadvantaged business greater access to the natural gas marketplace. Currently, Union Bank of California and Bank of America in California are offering this type of financial instrument.

Issued on January 13, 1999